



Flexible Benefit Plan and Health Reimbursement Plan (HRA) Owner Definitions and Eligibility Requirements

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C-Corporation, Non-Profit Organization and Government Entities

C-corporation owners and their families are eligible to participate in Flexible Benefit Plans and HRA Plans. They are considered to be W-2 common law employees. However, based on the Key Employee definitions, owners may be limited in their pre-tax participation based on Discrimination Testing requirements. Key employees, defined as owners and officers (see Key Employee Definitions) cannot have more than 25% of the total pre-tax benefits provided under a Flexible Benefit Plan. Example: \$10,000 in premium, dependent care and health care expenses are reimbursed or paid through the Flexible Benefit Plan in a given plan year. No more than \$2,500 of the \$10,000 total amount can be paid to the Key Employees combined.

Discrimination testing for HRA plans don't operate this way. HRA plans must be non-discriminatory in design – however, there is no testing based on who actually receives payment from the HRA plan each plan year. Therefore a Key employee could be the only recipient of HRA payments in a given plan year without concern; so long as the HRA plan design is non-discriminatory.

Non-profit organizations have no owners; however, they can still have Key employees who are officers and can still experience testing problems. If no employee meets the Key employee definition based on income and job description, they may still have a Key employee based on “facts and circumstances” definitions. Government employees are not owners and are not considered to be Key employees; therefore government groups do not have to comply with Key employee testing. However, Highly-Compensated Dependent Care Testing applies.

S-Corporations, LLCs and LLPs

Anyone who is a more than 2% owner of an S-corporation, LLC or LLP is not considered to be a W-2 common law employee, but rather a self-employed individual for tax purposes. Company profits and losses for these entities are passed on to the owners and taxed at their individual tax rates; making these owners non-W-2 common law employees for the purpose of Flex Plan and HRA Plan participation. Owners of these business entities are not eligible to participate in the Flex Plan nor are they eligible to participate in an HRA Plan.

Definitions of owners include anyone who is a more than 2% owner, their spouses, ascending and descending family members (parents, children and grandchildren). Under the “attribution rules” family members in these categories are counted as owners even when they own no stock in the company. Your tax counsel or CPA can help you determine who, under the attribution rules, will be ineligible to participate in these plans. However, these plans can be offered to your non-owner W-2 common law employees.

Sole Proprietorships and Partnerships

Sole proprietors and partners are not considered W-2 Common Law employees and are not eligible to participate in a Flex Plan or HRA Plan. However, the spouse of the sole proprietor or partner is eligible to participate in the plan if: the spouse is a true W-2 common law employee of the company, meets the eligibility requirements within the plan design and has no ownership interest in the company. However, the spouse of the owner is always considered a Key Employee and therefore the 25% Key Employee Test can create testing problems for the small proprietorship or partnership.